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July 15, 2019

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Re: Control and Divestiture Proceedings (Regulations Y and LL; Docket No. R-1662; RIN 7100-AF 49)

Dear Ms. Misback:

The Independent Community Bankers of America (ICBA)¹ appreciates the opportunity to comment on a proposal (the “Proposal”) that would revise the Federal Reserve’s regulations related to determinations of whether a company has the ability to exercise a controlling influence over another company for purposes of the Bank Holding Company Act or the Home Owners’ Loan Act. To clarify the Federal Reserve’s position, the Proposal would significantly expand the number of presumptions for use in such determinations and codify them as part of Federal Reserve Regulation Y and Federal Reserve Regulation LL.

Background

The Federal Reserve is seeking comment on proposed revisions to its rules regarding the definition of “control” under the Bank Holding Company Act (“BHCA”) and the Home Owners’ Loan Act (“HOLA”). There are three parts to the control test under the BHCA.² A company has control over another company if the first company (i) directly or indirectly or acting through one or more other persons owns, controls, or has the power to vote 25 percent or more of any class of voting securities of the other company; (ii) controls in any manner the election of a majority of the directors of the other company; or (iii) directly or indirectly exercises a controlling influence over the management or policies of the other company. HOLA includes a substantially similar definition of control.

¹ The Independent Community Bankers of America® creates and promotes an environment where community banks flourish. With more than 52,000 locations nationwide, community banks constitute 99 percent of all banks, employ more than 760,000 Americans and are the only physical banking presence in one in five U.S. counties. Holding more than \$4.9 trillion in assets, \$3.9 trillion in deposits, and \$3.4 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers’ dreams in communities throughout America. For more information, visit ICBA’s website at www.icba.org.

² See 12 U.S.C. 1841 et seq.

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Although the first two parts of the test are bright-line standards, the third part of the definition of control is a facts and circumstances determination by the Federal Reserve. In the Federal Reserve Board's opinion, a significant minority investment in a bank (i.e., one that is between 5 percent and 25 percent of the voting shares of the bank) can and often does, raise questions regarding whether the investor will be able to exercise a controlling influence over the management or policies of the target company. Consequently, because it is a facts and circumstances determination, it is often difficult for investors as well as banks to figure out when an investment that constitutes less than 25% of the voting shares of a bank is considered controlling or noncontrolling.

Since 1970 when the "control" definition of the BHCA was last amended, the Federal Reserve Board (the "Board") has issued a substantial amount of guidance regarding when an equity investment becomes a controlling interest. In 2008, the Federal Reserve attempted to consolidate and clarify its views by issuing a Policy Statement. In the 2008 Policy Statement, the Board stated that it had reviewed its experience with (1) director interlocks, (2) limits on the amount of nonvoting shares that could be held in combination with voting shares, and (3) the scope of discussions that minority investors could have with management of the banking organization and confirmed that a determination of whether an investor could exercise a controlling influence over a banking organization depended on the consideration of all the facts and circumstances of each case. In the 2008 Policy Statement, the Board provided some guidance on certain types of relationships that generally would not raise controlling influence concerns but was not clear enough with respect to situations where an investor could have a controlling influence.

ICBA's Comments

ICBA agrees with the Federal Reserve that the Proposal will enhance transparency and improve consistency of outcomes for controlling influence questions under the BHCA and the HOLA. Currently, the definitions of "control" under the BHCA and HOLA are not only confusing to investors but also to many community banks. We believe the proposed presumptions of control will not only clarify for investors when they have met the definition of "control" under the BHCA and HOLA but will also assist the Federal Reserve in conducting hearings or other proceedings under both laws. These presumptions will be a significant improvement over the current and often ambiguous guidance concerning "control."

Under current procedures as well as under the Proposal, the Federal Reserve will not find that a company "controls" another company unless the first company triggers a presumption of control with respect to the second company. A company that receives a preliminary determination of control must respond within 30 days with (1) a plan to terminate the control relationship, (2) an application for the Federal Reserve's approval to have control, or (3) a response contesting the preliminary determination, setting forth supporting facts and circumstances, and, if desired, requesting a hearing or other proceeding. According to the Federal Reserve, the proposed presumptions would apply at such a hearing or other proceeding and after considering all the relevant facts and circumstances including information gathered during the hearing or other proceeding, the Board would issue a final order stating its determination on controlling influence.

The Proposal incorporates many of the Board’s common historical considerations for assessing whether a company has the power to exercise a controlling influence over the management or policies of another company. The rebuttable presumptions of control would be based on the types and levels of relationships that the Board historically has viewed as allowing one company to have the power to exercise a controlling influence over another company. These would include (1) the size of the first company’s voting equity investment in the second company, (2) the size of the first company’s total equity investment in the second company, (3) the first company’s rights to director representation and committee representation on the board of directors of the second company, (4) the first company’s use of proxy solicitation with respect to the second company, (5) management, employee, or director interlocks between the companies, (6) covenants or other agreements that allow the first company to influence or restrict management or operation decisions of the second company, and (7) the scope of the business relationships between the companies.

The presumptions would be a sliding scale test that is keyed off of three levels of voting ownership: 5 percent, 10 percent, and 15 percent. While the Proposal does not cover all facts and circumstances that could potentially relate to controlling influence, it does cover most of the common ownership issues and certainly most of the situations that involve community banks particularly when shareholder activists are involved. For example, at the 5 percent level of voting ownership, the Proposal says that the first company is presumed to control the second company if, in addition to owning 5 percent of the voting securities, (1) director representatives of the first company comprise 25 percent or more of the board of directors of the second company or (2) an employee or director of the first company serves as CEO of the second company, or (3) the first company enters into transactions or has business relationships with the second company that generate in the aggregate 10 percent or more of the total annual revenues or expenses of the first company or the second company, or (4) the first company has any limiting contractual rights with respect to the second company. At the 10 percent or 15 percent level of voting ownership, the presumptions are triggered by fewer relationships. For example, at the 15 percent level, if the first company has just one director representative on the board of directors of the second company, there is a presumption of control. We applaud the Federal Reserve for spelling out the rebuttable presumptions of “non-control” when the first company controls less than 10 percent of voting securities of the second company.

In short, ICBA believes the Proposal is very comprehensive and provides welcomed transparency and clarification regarding the definition of “control” under the BHCA and the tiering of restrictions based on the first company’s level of ownership of the second company. The BHCA was intended to ensure that companies that acquire control of banks have the financial strength and managerial ability to exercise control in a safe and sound manner. The BHCA was also intended to separate banking from commerce by preventing companies with commercial interests from exercising control over banking organizations and by restricting the non-banking activities of banking organizations. Once implemented, we believe the Proposal will assist the Federal Reserve with fulfilling both those purposes. It will also significantly help both investors and community banks with understanding Regulation Y and Regulation LL and the facts and circumstances that the Federal Reserve considers most relevant when assessing controlling influence.

ICBA appreciates the opportunity to comment on the Proposal. If you have any questions or would like additional information, please do not hesitate to contact me at (202) 821-4431 or Chris.Cole@icba.org.

Sincerely,
/s/ Christopher Cole

Christopher Cole
Executive Vice President and Senior Regulatory Counsel